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modified in a written partnership agreement that specifies the details of capital contributions, management, sharing of profits and losses, rights and obligations, terms of property ownership, termination and dissolution, and buy/sell agreements.

A partnership files a federal information tax return (Form 1065) annually. Each partner receives a Schedule K-1, which provides information about his or her share of partnership income, credits, deductions, and other information. All income flows through and is taxed to the individual partners. A partnership interest is personal to the partner. The partnership is dissolved by the death of a partner or by the sale of a partnership share. While the spouse of a deceased partner is usually entitled to payment for the deceased partner's equity in the enterprise, the spouse is not entitled to participate in the partnership. Law firms and accounting practices were once operated almost exclusively as partnerships, although other models have become more prevalent in the past few decades.

A limited partnership has the characteristics of both a partnership and a corporation. It is used when some partners want neither management responsibilities nor unlimited liability for the business venture. Limited partnerships are sometimes used for investments sold to the public.

North Carolina has adopted the Revised Uniform Limited Partnership Act (RULPA). Under this statute, a limited partnership is formed by at least one general partner and one or more limited partners. The general partner manages the partnership and has full personal liability for any debts incurred by the partnership. Limited partners contribute cash or other property, and their liability for partnership debts is limited to the amount of their investment in the venture. Limited partners do not participate in the management of the partnership. A limited partnership also files an information tax return, but income is taxed to all the individual partners according to the distribution of profits specified in the partnership agreement.

Also governed by RULPA are family limited partnerships. These partnerships are generally restricted, by written agreement, to a defined range of family members. Family limited partnerships may be used to keep business assets in the family; protect the business from the consequences of divorce, death, and disability; provide for better organization and management of the business; and reduce estate taxes through valuation discounts and other means.

## **Limited Liability Company**

A limited liability company (LLC) is a distinct entity that is a hybrid of a partnership and a corporation. North Carolina law authorized this type of business entity effective October 1, 1993. It may be treated as a partnership for tax purposes. The IRS allows an LLC to choose ("check the box") whether to be taxed as a corporation or as a partnership. As with a corporation, the members have limited liability for debts of the LLC.

This business entity offers more flexibility because of its hybrid nature. The LLC is not allowed to have an unlimited life, as a corporation is, but it may have orderly transfer provisions. Membership interests are not freely transferable without the consent of all other members, but a member may assign his or her economic rights, but not voting rights. The statute has been amended to allow for a one-member LLC.

This business entity is often used in estate planning because it can be an efficient way to transfer assets over time to the next generation. It may also generate valuation discounts that can reduce the value of the business in the gross estate and therefore reduce estate taxes. Valuation discounts typically result from restrictions on sales placed upon owners of interests in the business and the minority owner status of some or all owners.

The LLC has the same limitations on liability as a corporation. The owners, like shareholders of a corporation, are not liable for the debts, torts, or other civil liabilities of the LLC. However, the limitations on liability, for owners in family-owned LLCs and shareholders in closely held corporations, are largely illusory. Because the business owners are also generally its operators, they are likely to incur personal liability in tort because it will be argued that their personal actions as a business operator or manager gave rise to the liability. Few lenders are willing to lend to LLCs and closely held corporations without the personal guarantees of their owners or shareholders.

## **Corporation**

Corporations are formed under state statutes. A corporation is a separate legal entity that has rights and liabilities separate from its shareholders. Shareholders of a corporation are liable for the debts of the corporation only to the extent of their investments in the corporation. Shareholders elect a